

CITY OF MONTEBELLO

Review Report

ADMINISTRATIVE AND INTERNAL ACCOUNTING CONTROLS

July 1, 2009, through June 30, 2010



JOHN CHIANG
California State Controller

December 2011



JOHN CHIANG
California State Controller

December 28, 2011

Art Barajas
Mayor of the City of Montebello
1600 West Beverly Boulevard
Montebello, CA 90640

Dear Mayor Barajas:

Enclosed is the report of the State Controller's Office review of the City of Montebello's administrative and internal accounting controls system. The review was conducted to assess the adequacy of the city's controls to safeguard public assets and to ensure proper use of public funds.

Our review found significant weaknesses with the City of Montebello's administrative and internal accounting control system. As a part of the review, we made an assessment of various aspects of the city's internal controls components and elements in accordance with standards adopted by the American Institute of Certified Public Accountants. Of the 74 control elements evaluated pertaining to internal control components, we found only eight (11%) where controls were considered to be adequate. In the areas under control environment related to integrity and ethical value, commitment to competence, and management and operating style, we found none of the 16 control elements to be adequate. The results of our review and evaluation of elements of internal control are included in this report as Appendix 1.

As a result of the significant control deficiencies, the potential for waste, fraud, and abuse of public resources is extremely high, and has led, at least in part, to the issues noted in the Findings and Recommendations section of our report.

The city should develop a comprehensive remedial plan to address these deficiencies. The plan should identify the tasks to be performed, milestones, and time frames for completion. We recommend that the Montebello City Council require periodic updates of the progress in implementing the remedial plan to be reported in public meetings.

In its response to our draft report, the city concurred with five of the eight findings, agreed with the majority of items in one finding, and disagreed with two findings, and requested that we eliminate these findings.

The city's response to our findings and our comments are incorporated into the body of the report. The city's entire response also is included as an attachment to this report.

If you have any questions, please contact Steve Mar, Chief, Local Governments Audits Bureau, at (916) 324-7226.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

JVB/wm

cc: Dr. Frank Gomez, Mayor Pro Tem
City of Montebello
William M. Molinari, Councilmember
Montebello City Council
Alberto Perez, Councilmember
Montebello City Council
Christina Cortez, Councilmember
Montebello City Council
Larry Kosmont, Interim City Administrator
City of Montebello
Keith Breskin, Interim Assistant City Administrator
City of Montebello
Francesca Schuyler, Director of Finance
City of Montebello

Contents

Review Report

Introduction	1
Background	3
Objectives, Scope, and Methodology	3
Conclusion	3
Views of Responsible Officials.....	4
Restricted Use	4
Findings and Recommendations.....	5
Appendix 1—Evaluation of Elements of Internal Control.....	23
Attachment—City’s Response to the Draft Audit Report	

Review Report

Introduction

The State Controller's Office (SCO) reviewed the City of Montebello's system of administrative and internal accounting controls for the period of July 1, 2009, through June 30, 2010. When necessary, we expanded our testing to include prior year transactions to follow up on issues identified through interviews of city officials and through our review of the work of the independent auditors and other audit reports.

On April 21, 2011, the SCO notified Interim City Administrator Peter Cosentini that the City of Montebello and the Montebello Redevelopment Agency have not complied with state law regarding the submittal of annual reports and independent audits, as follows:

- City of Montebello—The Annual Report of Financial Transactions of Cities for 2009-10, required by Government Code section 53891, was not filed.
- Montebello Redevelopment Agency (RDA)—The Annual Report of Financial Transactions of Redevelopment Agencies for 2009-10, required by Health and Safety Code section 33080.1, was incomplete.
- City of Montebello—The Single Audit Report was not submitted by the due date of March 31, 2011.

Both the city and the RDA have been delinquent in providing these reports in past years. These delays in compliance have raised concerns about the reliability and accuracy of the information in the reports. This was of a particular concern in light of this and other information about the city's and RDA's financial practices:

- The 2008-09 single audit of the City of Montebello identified several material or significant deficiencies in the city's internal controls over financial reporting and compliance. Several of the deficiencies had been noted in previous audits and still had not been addressed.
- Recent presentations to the Montebello City Council have contained the following information:
 - ✓ Restricted funds under the control of the city have been used to pay for the city's general purpose administrative costs.
 - ✓ Reimbursement of the restricted fund loans have been made possible only by loans of \$14.8 million from funds that are supposed to be used for redevelopment programs.
 - ✓ Loans of some restricted funds can be made as long as they are paid back by the end of the fiscal year or sooner, as necessary to address required expenditures of the fund or agency from which they were borrowed. However, that is not always the case.
 - ✓ The use of restricted funds and redevelopment loans are the only reason the city has avoided deficit spending in its general fund.

- ✓ Without actions to reduce expenditures or increase revenue, the city was expected to run out of cash by October 2011. Among other things, this would mean that city would not meet financial obligations, including paying employees.
- The city recently was made aware that two “off-the-books” RDA bank accounts had been in existence for more than ten years without the city’s knowledge. It is not clear whether they were reflected in the prior Annual Report of Financial Transactions for Cities submitted by the city.
- Council Member Christina Cortez has expressed concerns in public meetings and verbally to staff members in my office about actions taken by the city in the past, particularly the loan of funds from the redevelopment agency. In addition, she raised concerns about the use of Housing and Urban Development (HUD) funding. We understand that a report from the Office of Inspector General at HUD concludes that the city may have to pay back nearly \$1.3 million.
- The Interim City Administrator resigned, effective May 13, 2011, because the Montebello City Council would not consider taking action in a timely manner to address the financial issues he raised.
- In addition, Council Member Frank Gomez made a public statement that the other Council Members were either “in denial” or “lacked the conviction to do anything to solve the problem.”

After considering the above information, the SCO concluded that there is reason to believe that the Annual Report of Financial Transactions by the City and the RDA are false, incomplete, or incorrect. Therefore, under Government Code section 12464(a), the SCO conducted an investigation to gather the information needed to validate the information provided for those reports for Fiscal Year (FY) 2009-10.

In addition, the SCO reviewed programs with State general or special funding and/or any federal funding passed through the State to the city or the RDA by a State agency. These additional activities also were conducted under Government Code section 12468, which authorizes the State Controller to “. . . regularly audit the apportionment and allocation by counties of property tax revenue . . .” and under Government Code section 12410, which authorizes the Controller to “. . . superintend the fiscal concerns of the state. The Controller shall audit all claims against the state, and may audit the disbursement of any state money, for correctness, legality, and for sufficient provisions of law for payment.” Our review focused on FY 2009-10 transactions; however, we also reviewed prior period transactions as necessary.

This report presents the results of findings and conclusions reached in the review of the city’s administrative and internal accounting controls system.

Separate reports were issued for our audit of the Special Gas Tax Street Improvement Fund and reviews of the Montebello Redevelopment Agency, and the City of Montebello’s state and federal expenditures.

Background

The City of Montebello is located in Los Angeles County, California. In 2007, the population of 64,695 lived in an area of 8.2 square miles. On October 16, 1920, Montebello was incorporated as the 35th of the present cities in Los Angeles County. The city conducts its operations as general law, Council/Administrator City.

Objectives, Scope, and Methodology

The objective of this review was to evaluate the City of Montebello's system of administrative and internal accounting controls to ensure:

- Effectiveness and efficiency of operations;
- Reliability of financial reporting;
- Compliance with applicable laws and regulations; and
- Adequate safeguard of public resources.

To accomplish our objective, we performed the following procedures:

- Evaluated the city's formal written internal policies and procedures.
- Conducted interviews with city employees and observed the city's business operations for the purpose of evaluating city-wide administrative and internal accounting controls.
- Reviewed the city's documentation and supporting financial records.
- On a limited basis, performed tests of transactions to ensure adherence with prescribed policies and procedures and to validate and test the effectiveness of controls.
- Assessed various aspects of the city's internal control components and elements in accordance with guidelines adopted by the American Institute of Certified Public Accountants.

Conclusion

Our review found significant weaknesses with the City of Montebello's administrative and internal accounting controls system. We found that the potential for waste, fraud, and abuse of public resources is extremely high due to numerous deficiencies noted in the Findings and Recommendations section of our report.

As a part of the review, we assessed various aspects of the city's internal control components and elements in accordance with standards adopted by the American Institute of Certified Public Accountants. Of the 74 control elements evaluated pertaining to internal control components, we found only eight (11%) where controls were considered to be adequate. The results of our review and evaluation of the elements of internal control are included in this report as Appendix 1.

The city should develop a comprehensive remedial plan to address these deficiencies. The plan should identify the tasks to be performed, and milestones and time frames for completion. We recommend that the Montebello City Council require periodic updates at public meetings of the progress in implementing the remedial plan.

**Views of
Responsible
Officials**

We conducted an exit conference on November 22, 2011, with Larry Kosmont, Interim City Administrator; Keith Breskin, Interim Assistant City Administrator; Francesca Tucker-Schuyler, Finance Director; and Andy Zageris, Accountant. At the exit conference, we stated that the final report will include the views of responsible officials.

The city provided its response to our draft report on December 9, 2011, and it is included in this report as an Attachment. In its response to our draft report, the city concurred with five of the eight findings, agreed with the majority of items in one finding, and disagreed with two findings requesting that we eliminate these findings.

After carefully reviewing and analyzing the city's response, we have found that the city did not provide any additional documentation within their response to change our findings. The city's response and the SCO's comment to each specific issue are included immediately following each issue.

The city's entire response is also included as an attachment to this report.

Restricted Use

This report is solely for the information and use of the City of Montebello and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record.

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

December 28, 2011

Findings and Recommendations

RESULTS OF ANALYSIS OF CITY'S ADMINISTRATIVE AND INTERNAL CONTROL SYSTEM

We found significant weaknesses in most aspects of the City of Montebello's administrative and internal accounting controls system. As part of the review, we selected 74 internal control elements based primarily on standards adopted by the American Institute of Certified Public Accountants. We then assessed the city's internal control policies and procedures against these internal control elements and found only eight (11%) where controls were considered to be adequate (see Appendix 1 for the results of our evaluation of internal control elements).

In the overarching components under control environment for integrity and ethical value, commitment to competence, and management and operating style, we found none of the 16 control elements to be adequate. Under such a weak control environment, the potential for waste, fraud, and abuse is extremely high. The **findings** described below all resulted, at least in part, from these deficiencies.

Recommendation

While there are specific recommendations to address the specific **findings** described below, we recommend that the city develop a comprehensive remedial plan to address the deficiencies noted in Appendix 1. The plan should identify the tasks to be performed, and milestones and time frames for completion. In addition, we recommend that the Montebello City Council require periodic updates at public meetings of the progress in implementing the remedial plan.

FINDING 1— Problems with personnel transactions and expenditure approvals

During the review, we identified the following examples where personnel transactions and expenditure approvals were handled inappropriately.

City actions may have increased the former City Administrator's pension above the level it should have been and this may constitute pension-spiking.

On March 14, 2007, the Montebello City Council voted to terminate the City Administrator effective April 15, 2007. The City Administrator contested the termination and was placed on administrative leave where he continued to receive his monthly salary of \$10,934. On November 2, 2007, he reached a termination settlement agreement with the city.

However, the termination settlement agreement was not implemented and the City Administrator continued to be on administrative leave, and continued to receive a monthly salary of \$10,934 until January 16, 2008. At that time the City Council, which had two new members as a result of a recall election, "rehired" the City Administrator. The City Administrator retained the salary he had been paid since his "termination" on April 14, 2007, including the payments he received between November 2, 2007, and January 16, 2008. In addition, the City Council raised the City Administrator's monthly salary to \$16,250 (an

increase of nearly 49%), effective immediately. The City Administrator was the only city official to receive a salary increase of this magnitude at that time and the increase greatly exceeded every previous increase granted to the City Administrator. (See the chart below for a comparison of the City Administrator's salary for the entire period of his employment at that level.) In addition, there was no explanation for such a large increase.

City Administrator's Salary:

Date	Position	Personnel Action	Monthly	Annually	Percent Change
12/30/2009	City Administrator	Service retirement	\$ 16,250	\$ 195,000	
01/16/2008	City Administrator	Salary increase	16,250	195,000	48.62%
07/01/2006	City Administrator	Salary increase	10,934	131,208	3.01%
07/01/2005	City Administrator	Salary increase	10,615	127,380	3.00%
07/01/2002	City Administrator	Salary increase	10,306	123,674	2.00%
07/01/2001	City Administrator	Salary increase	10,104	121,248	2.00%
10/26/2000	City Administrator	Salary increase	9,906	118,872	3.40%
01/01/2000	City Administrator	Salary increase	9,580	114,960	1.40%
07/01/1999	City Administrator	Salary increase	9,448	113,376	3.34%
01/01/1998	City Administrator	Salary increase	9,142	109,709	3.40%
11/05/1997	City Administrator	Salary increase	8,842	106,102	7.12%
07/01/1991	City Administrator	Salary increase	8,254	99,049	5.37%
05/09/1990	City Administrator	Salary increase	7,833	94,000	6.58%
05/13/1989	City Administrator	Promotion to City Administrator	7,350	88,200	

The City Administrator retired approximately two years later on December 30, 2009. We estimate that the former City Administrator will receive an increase of more than \$4,000 per month in pension payments from the California Public Employees' Retirement System (CalPERS) for two reasons: (1) the increase in salary effective January 16, 2008, and (2) the city reported the time covered by his termination settlement agreement and the time between the effective date of his termination settlement agreement and his rehiring by the City Council to CalPERS as eligible service time in calculating his pension.

There appears to be no support for counting the period between November 2, 2007, and January 16, 2008, as eligible for CalPERS credit. Also, as the former City Administrator was the only official who received a salary increase of this magnitude, and the increase occurred near the end of his employment status, it may constitute pension-spiking. Both issues merit further review by CalPERS.

In addition, it appears that one reason for results described above, is that the Human Resources office was not made aware of the various actions described above. As a result, the Human Resources office continued to treat the City Administrator as a full-time employee during the entire period.

Recommendation

The city should ensure that information is communicated to the appropriate departments in a timely manner and follow up on appropriate actions when necessary. Additionally, the city should contact CalPERS to discuss and resolve this issue.

Violation of Tax Reporting Requirements

The city gave a retention payment (bonus) to all employees under a Memorandum of Understanding (MOU) with all employee groups during FY 2007-08. The MOUs provided payments of \$5,000 to full-time employees and \$2,500 to part-time employees. The total amount of retention payments was \$2,002,500. These payments were reported to the employees and the Internal Revenue Service (IRS) on Form 1099. In addition, the city reported the amounts on Form 1099 as "miscellaneous income."

Additionally, stipends to city council members and other committee members for various board and committee meetings have also been, and continue to be, reported on Form 1099 and designated as "miscellaneous income." For example, one council member received \$2,235 in stipends for the 2010 calendar year for various board meetings.

In both instances, the city should have reported the bonuses and stipends on Form W-2, not on Form 1099.

The IRS states, "Generally, any individual who serves as a public officer is an employee of the government for whom he or she serves. Therefore, the government entity is responsible for withholding and paying federal income tax, social security and Medicare taxes, and issue a Form W-2, Wage and Tax Statement, to the public official." The IRS further states, that, "although there is no precise definition for the term "public official" or "public officer," the courts have generally held that anyone who exercises significant authority pursuant to public laws is a public officer. This includes any official who administers or enforces public laws, whether the individual is elected by the public or appointed to an office."

While state and federal taxes eventually will be collected when the employee files the Form 1099 with his/her annual tax forms, the avoidance of required withholding means that both levels of government do not have access to revenues as required by state and federal law.

Also, by reporting the payments on the Form 1099, the city did not deduct and pay the employee's share of other payroll taxes (e.g., Social Security and Medicare) or the employer's share of such payroll taxes.

Recommendation

The city should adopt policies to ensure that future bonuses, as well as ongoing stipends, are reported as required. In addition, the city should contact the appropriate taxing agencies to correct any errors with previous reporting.

Inappropriate Treatment of Severance Pay

The city entered into a severance and mutual separation agreement with a previous Director of Community Development on July 18, 2006. This severance agreement provided the employee with 12 months of severance pay which included salary, benefits, and retirement payments to CalPERS. The employee effectively was terminated from the city payroll on August 26, 2007, more than 12 months later. CalPERS sent a letter to the City of Montebello on January 4, 2008, advising that the severance agreement was settlement pay, and therefore was not reportable to CalPERS. Had CalPERS failed to uncover this reporting discrepancy, the employee would have received an extra year of service credit to which he was not entitled.

The August 2007 CalPERS letter instructed the city to reverse all payroll entries made under the severance agreement. City staff members did not make any adjustments or reverse these payroll entries until June 2011, after we brought it to their attention during the review.

Recommendation

The city should ensure that appropriate actions are addressed in a timely manner.

Override of Petty Cash Controls

During our testing of petty cash, we noted that a previous City Administrator, on numerous occasions, approved his own petty cash reimbursements for questionable expenses, as noted in our Montebello Redevelopment Agency Review Report, dated September 22, 2011, Finding 1.

In addition, the SCO found an instance where a police officer circumvented petty cash policy. The police officer made a purchase of food for approximately \$250 for a city function. The reimbursement claim form clearly states that petty cash is only to be used for items up to \$100. Instead, the officer had the restaurant break up the approximately \$250 purchase into three different receipts.

Recommendation

The city should ensure that policies and procedures relating to petty cash controls are updated when appropriate and enforced consistently.

Conflict of Interest and Lack of Competitive Bidding for Engineering Contract and Projects

In the recently issued report of our review of state and federal expenditures, we noted several problems with the contract awarded to Advanced Applied Engineering (AAE) to act as the City Engineer and engineering projects AAE awarded to itself. We noted that the continued extension of the engineering contract past the date of a City Ordinance requiring competitive bidding (adopted in 2007) violated the intent of that ordinance. In addition, we pointed out that any engineering projects

exceeding \$50,000 awarded after the new ordinance should have been competitively bid. Also, we noted that AAE's ability to provide oversight of any awards to itself, created the potential for conflicts of interest.

Recommendation

The city should comply with its own ordinance by taking the following actions:

- Set an end date for the current engineering contract and develop and implement a competitive bid process to award a new contract.
- Require that all future engineering services for capital improvement projects over \$50,000 be competitively bid.
- When engineering services for capital improvement projects are awarded to AAE, or any subsequent contractor, establish an independent review for the work performed and payment of invoices.

By complying with its own ordinances, the city will remove any appearance of conflict of interest or lack of independence in its award and oversight of capital improvement projects and its engineering program. In addition, it will ensure that the city is getting the most competitive price for such services.

City's Response

- **City actions may have increased the former City Administrator's pension above the level it should have been and this may constitute pension-spiking**

A review of City files confirms that a prior City Council executed a separation agreement on November 2, 2007, to terminate the employment of a former City Administrator and that former City staff failed to properly process the termination. When current City executive staff learned of this issue in 2011, City staff immediately began working with CalPERS to correct deficiently-reported earnings to CalPERS from the period the prior City Administrator was terminated to when he was rehired by the City on January 16, 2008. Subsequently a Notice of Change was sent to the City to reverse payroll for the applicable period of time. City Payroll staff have taken steps to make the corrected reversal, and have been in contact with CalPERS to accommodate the reversal which has been delayed due to CalPERS' current systems upgrade.

To ensure that this issue is avoided in the future, City executive staff will recommend a Personnel Procedure to be adopted by the City Council, which will provide for a written communication process as applicable to changes in the employment status with employees, including, but not limited to, the City Administrator, so that those changes can be properly processed in a timely manner.

- **Violation of Tax Reporting Requirements**

The City concurs with this finding, and remains fully committed to complying with federal and state tax reporting requirements and utilizing the proper reporting forms. The City will ensure that future bonuses as well as ongoing stipends are reported as required. The City will contact the appropriate taxing agencies to correct any errors with previous reporting as deemed necessary.

- **Inappropriate Treatment of Severance Pay**

The City acknowledges that on July 18, 2006, the City and the former Director of Community Development entered into a separation agreement to include severance and other benefits. Further, on January 4, 2008, CalPERS sent the City a letter indicating that the compensation reported from July 2006 to June 2007 was final settlement pay and should not have been reportable to CalPERS as compensation earnable. Although this issue was not corrected at that time, current City executive staff promptly reversed the transaction on June 13, 2011 when it was first brought to their attention. As such, all applicable erroneously-reported compensation has been corrected with CalPERS.

To avoid this issue in the future, City executive staff will work closely together to correct any reporting errors with CalPERS in a timely manner. City executive staff will recommend a Personnel Procedure to be adopted by the City Council, which will provide for a written communication process as applicable to changes in the employment status with employees, including, but not limited to, the City Administrator, so that those changes can be properly processed in a timely manner. In the Interim City Administrator's recent Management Summary Report, which was presented to the City Council on November 9, 2011, the Interim City Administrator's recommendation was to improve internal operating systems.

- **Override of Petty Cash Controls**

The City concurs with this finding and will ensure that policies and procedures related to petty cash controls are updated and enforced consistently.

- **Conflict of Interest and Lack of Competitive Bidding for Engineering Contract and Projects**

The City acknowledges this finding, and is currently in the process of re-evaluating its current agreement for engineering services. In the Interim City Administrator's recent Management Summary Report, which was presented to the City Council on November 9, 2011, the Interim City Administrator's recommendation was to bid the contract after consulting an external engineering expert to review the existing practices and make recommendations. A copy of the updated Management Summary Report is attached as **Exhibit A**. In fact, the City recently issued a Request for Proposals for such an expert to review the current engineering processes and the agreement for engineering services. It is anticipated that the expert, once retained, will complete its analysis by February 2012.

As noted by the SCO, this finding regarding the City's award of the engineering services contract to Advanced Applied Engineering, Inc. ("AAE") was previously identified in the review report of state and federal expenditures. In response to that report, the City provided a lengthy rebuttal to the SCO's findings. The City expressly informed the SCO that to apply a later-adopted ordinance *to the terms* of an existing contract, potentially placed the City in unnecessary jeopardy. In particular, the automatic extension provision of the contract *was part of the contract* that was awarded in January 2005, *two years prior* to the adoption by the City Council of Ordinance No. 2304, which established Chapter 3.21 ("Contracts for Professional and Special Services") of the Montebello Municipal Code ("MMC"). Chapter 3.21 does not expressly apply retroactively, and if the City took the position that Chapter 3.21 applied to the automatic extension provision of the contract (without any express intent in the ordinance itself), it is possible the City may be subject to a claim that it breached the agreement, or that the law itself impaired the obligations of a contract.

It appears to the City that the better solution is to follow the process City staff has already initiated, which is to select an engineering expert to provide recommendations, and then subsequently improve engineering and public works procedures by adopting a competitive bid process as directed by a thorough analysis of an independent expert. Although the City maintains its position that the MMC Chapter 3.21 does not apply to the terms of the engineering services contract, the City acknowledges the fact that certain engineering projects that exceeded \$50,000 and that arose after the implementation of Chapter 3.21 should have been competitively bid. The City is committed to receiving the best competitive prices for its capital improvement projects, has taken affirmative steps in evaluating the current agreement with AAE, and will be making recommendations to overall engineering processes as well as going out to bid for its engineering services before the end of the current fiscal year.

In summary, the City acknowledges and concurs with the majority of Finding 1, has taken affirmative steps to addressing the various issues raised therein, and will ensure that its policies and procedures are both updated and enforced.

SCO's Comment

The city concurs with the finding.

**FINDING 2—
Cash impairment in the
city's investment pool**

In the recently issued reports of our review of State and Federal expenditures as well as of our gas tax audit, we noted that the city's process for maintaining General Fund cash in an investment pool with cash from other funds, including restricted funds, creates the potential for these restricted funds to be impaired. During our review, we noted that the city's operating costs of the General Fund were paid for by funds from the city's investment pool and that the General Fund cash balances were negative for the entire FY 2009-10 with the exception of June 2010. At year-end, the city made journal entries and transferred cash between the General Fund and other funds to eliminate the negative cash balance for financial statement purposes. The city has employed this practice in past years. The General Fund had negative cash balances, for all months in FY 2010-11 and has continued into FY 2011-12.

When the General Fund cash balances are negative, it means that the cash from other funds in the investment pool, including restricted funds, is being used to pay for General Fund-related expenditures. Thus, any of these other funds that have a positive cash balance are potentially impaired, and may not be able to make timely payments of required expenditures that should be made from those funds.

While it is clear that the cash in the investment pool from the other funds, including restricted funds, was used to pay for goods and services that should have been paid for by the General Fund, the city could not document which fund(s), restricted or not, were used for this purpose.

Recommendation

The city should develop and implement policies and procedures to ensure that it does not impair other funds' cash, especially the restricted funds, by using them to pay for general operating costs that should be paid from the General Fund. Additionally, the finance department should determine each fund's balance in the investment pool and ensure that withdrawals from that pool are only used to address costs that can be paid from each fund. In addition, to the extent that it is allowable to use cash from one fund to pay for expenditures that should be paid from another, such loans should be documented and ensure that the loan is repaid as soon as required, with interest.

City's Response

The City has responded, previously, to the matter of cash impairment in response to prior SCO reports. The matter of the use of restricted funds was corrected by the City in February of 2011. The City can document that there was no cash impairment since the City's investment portfolio indicates that it exceeded the cash balances which are deemed restricted. Additionally, as of March 2011, the monthly investment reports submitted to the Council and the City's Investment Committee includes a balance that separates the general fund balance of the pooled cash from that of the restricted funds.

The City's accounting system records deposits and disbursements by fund. Therefore the cash balances for each specific fund is available. Please see response to Finding 3 for additional comments.

There was no cash impairment; therefore, the SCO should eliminate this finding.

SCO's Comment

The SCO's prior reports of the Gas Tax Fund and State and Federal Expenditures disclosed cash impairment. The city's responses to cash impairment findings in those reports did not provide sufficient documentation of the city's assertion that the General Fund did not impair other restricted funds during FY 2009-10. As such, we did not eliminate the finding in those two reports.

The city's current response does not provide sufficient documentation of city's assertions. Basically, the city states that it made corrections to the use of restricted funds in February 2011 and is accounting for General Fund cash balances separately from the restricted funds in the pooled cash balances effective March 2011. The city is commended for making the necessary corrections; however, this did not address the noted cash impairment during FY 2009-10.

The finding remains the same.

**FINDING 3—
Questions about the
accuracy, reliability,
and timeliness of data in
the city's accounting
system**

Significant control deficiencies resulted in errors in accounting for and expending funds, including funds from state and federal governments. Specifically, the General Ledger balances produced by Government e-Management Solutions, Inc. (GEMS) are not reliable. Due to the delay in closing out FY 2009-10, the fund balances were not carried forward to FY 2010-11 until July 2011. During FY 2010-11, GEMS continually reported balances that did not reflect the funds carried over from the previous year until well into the subsequent year. City staff members had to make manual adjustments to the data to reflect information. In addition, because of the delay in approving budgets for FY 2009-10 and FY 2010-11, comparisons of expenditures were made to estimates of the amount that would eventually be approved.

The State Controller's Office (SCO) has identified several factors that have created the deficiencies described above. These factors include:

Implementation of a New Accounting System

The city installed a new financial system in 2007 called GEMS: It appears that staff members do not have a sufficient understanding of the system and how to use it properly. In part, this is because there has been a significant turnover in staff.

Inadequate Documentation of Overall Accounting Procedures and Processes

Although most employees had information on the procedures and processes for their particular assignment, there is no documentation of the overall procedures and processes of the accounting system. Therefore, most staff members do not have any understanding of the accounting system except as it relates to their assigned duties.

Delays in Closing of Financial Records

The city did not close its FY 2009-10 financial records until July 2011. Timely closing of financial records should be performed within three to six months after year-end.

Delayed Adoption of a Budget

During FY 2009-10, the city operated on the previous year's budget until the budget was formally adopted in April 2010. During FY 2010-11, the city operated on a proposed budget which was not formally adopted until June 2011.

Insufficient Information Supporting Journal Vouchers

The Journal Vouchers (JV) prepared by the city lack adequate information as to the purpose of the transactions. A JV is a document that authorizes entries into the accounting system such as transferring amounts between accounts and reclassifying or correcting data in the General Ledger system. JVs are an integral part of the audit trail and should be prepared with adequate information and include supporting documentation. A typical JV prepared by the city only includes the General Ledger account numbers affected by the transaction, the debit and credit amounts, and a brief reason, such as "to record adjustment" at the end of a batch of JVs. In addition, the JVs do not have sufficient supporting documentation.

Recommendation

The city should adopt policies and procedures to address the problems discussed above. Specifically, this should include the following: (1) develop a comprehensive list of policies and procedures for all financial processes and provide training to staff; (2) perform timely year-end closing of financial records; (3) ensure that JVs are adequately supported; and (4) adopt of the city's budget in a timely manner.

City's Response

The general ledger balances produced by Government e-Management Solutions, Inc. (GEMS), the City's accounting system, can be relied upon, if the information posted is correct. It has recently been determined that the information posted into the accounting system in July 2008 and July 2009, by the former finance director and former accountant was incorrect. Ending balances of June 30, 2008 were duplicated via journal entry for all balance sheet accounts, for all funds, in July 2008, which overstated assets, liabilities and fund balances. Ending balances of June 30, 2009 were duplicated, again, via journal entry for all balance sheet accounts, for all funds, further corrupting the integrity of the financial data in the City's general ledger. Ad hoc reporting systems were used to generate the trial balance report to compensate for the incorrect balances of the general ledger.

Upon discovery of the duplicated entries, corrective actions were taken to reverse the duplications and to provide the current auditors with a correct general ledger that can be relied upon to conduct the annual audit.

- **Implementation of a New Accounting System**

Although the City concurs that there has been recent staff turnover in the Finance Department, such turnover is not the reason for the improper use and implementation of the new accounting software. The new software was implemented in July of 2007 and staff turnover did not occur until Fiscal Year 2010-11. Once the software was implemented, the former finance director and the former accountant had the responsibility to ensure that there was proper documentation to support the balances as represented in the general ledger. It has become apparent that the system was not set up properly from the onset and errors were made in transactions, as noted above.

Moreover, based on the various prior SCO's audits, as well the Management Systems Report from Kosmont Companies (the City's independent consulting firm that has provided Interim City management and financial turnaround services), the City acknowledges its need to implement a better accounting structure. Specifically, an improved Accounting System was listed as the first "Wish-List" item in the Interim City Administrator's updated Management Summary Report (attached as **Exhibit A**). The City agrees that a specific accounting module must be identified, and that personnel must be trained on using the module.

- **Inadequate Documentation of Overall Accounting Procedures and Processes**

Documentation of the overall procedures and processes of the accounting system does exist. The City acknowledges that a climate existed whereby staff's understanding in the overall procedures and processes was limited. The City will examine and evaluate methodologies to increase understanding and participation.

- **Delays in Closing of Financial Records**

The City acknowledges that it did not close its FY 2009-10 financial records within six months after year end. The audit for FY 2009-10 was delayed due to various issues including incorrect and insufficient documentation provided by the former finance director and former accountant to the auditors. Once the audit was completed, in June 2011, the current finance director closed the books.

- **Delayed Adoption of a Budget**

The City concurs with this factor. To correct this deficiency, the first order of business of current Interim City Administrator Larry Kosmont was to obtain formal adoption of the FY 2010-11 budget by the City Council, which took place in June 2011, six weeks after Kosmont Companies initiated its assignment as Interim City Administrator.

- **Insufficient Information Supporting Journal Vouchers**

The City concurs with this observation. The former accountant, historically, did not provide sufficient documentation and detail to the various journal entries prepared. It appears that in prior years, the former Finance Director did not require or enforce sufficient

documentation as he signed off on many of these journal entries. The entries prepared by the former finance director did not have adequate documentation as well. This further delayed of the FY 2009-10 audit and the closing of the books.

In sum, the City concurs with a majority of the “factors” in Finding 3, and has taken corrective actions to address many of the issues raised therein. However, the City disputes that the documentation of the overall procedures and processes of the accounting system is inadequate.

SCO’s Comment

The finding is not whether or not there was documentation of particular process but the lack of adequate documentation of the overall procedures and processes. The fact remains that the city acknowledges that a climate existed where staff’s understanding in the overall procedures and processes was limited. The city further states that it will examine and evaluate methodologies to increase understanding and participation. This can in part be attributed to the lack of adequate documentation.

The finding remains as stated.

FINDING 4— Significant problems with the city’s cash reconciliation process

Our review of the city’s bank reconciliation process revealed the following issues that prevent proper reconciliation:

Differences Between Bank Statement and General Ledger Amounts

The city’s cash reconciliation at June 30, 2010, included an unreconciled amount of approximately \$300,000. While the city and its external auditor deemed this amount immaterial to impact fair presentation of the cash position in the annual audit for FY 2009-10, the city had not been able to reconcile this amount, which could be missing or unrecorded transactions in revenue, expenditures, assets, liabilities, and fund equities accounts.

Timeliness

For FY 2010-11, the city was 11 months in arrears in its bank reconciliations. The last completed reconciliation by the city was during July 2010. As a result, the city had to resort to estimates and by assessing bank information daily to determine available cash prior to making payments for payroll, vendors, debt services, and capital outlay. Timely information on cash is vital for all city functions. By relying on bank inquiries to determine the available cash, the city may issue payments for which there may be insufficient funds (for example, outstanding checks could be cashed sooner than expected). During our review, we noted the lack of timely financial information resulted in the city’s transit department’s decision to maintain its own records to account for cash, revenue, billing/accounts receivable, expense/accounts payable, and capital outlay. The city stated that it has completed the bank reconciliations through July 2010, which puts it a full year behind in this very important process. It should also be noted that the city has been aware of this issue for several years and has not taken action to address

it. The independent auditor's financial reports for FY 2008 and 2009 disclosed this problem and recommended that the city take action to address it.

Unreconciled Outstanding Checks

Issues with outstanding checks began during 2007, when the city implemented GEMS, a new accounting system. During the transmission of checking data to Bank of the West, the checks' six-digit number was modified to include two additional digits because transfer data requires an eight-digit number. The additional two zeroes attached to the end of the check number prevented cancellation of the checks from being reflected on the records. As a result, approximately \$24,000,000 in checks issued since implementation of GEMS was listed as outstanding, even though most checks had been cashed. An employee within the city's finance department was aware of the issue but did not report this to city management until SCO staff pointed this out. During this entire time, these outstanding checks were included as reconciling items for those bank statements that had been reconciled.

Untimely Recording of Corrections to Payroll Checks

Regular payroll processing is performed in the payroll system within GEMS which allows for such data to be posted directly into the city's General Ledger. Additionally, there is a separate process to record replacement of payroll checks and other special issuance of payroll-related checks; however, the SCO noted that three of these special payroll batches had not been posted until we notified the city of this problem.

Missing Deposit Slips for the City Transit Department

The SCO noted several ongoing problems where deposit slips for coin transit fares were missing. An armored car service was hired to bring coin deposits directly to the bank along with deposit slips; however, some deposit slips were missing for deposits made by the service. In addition, while the transit department sends its transit fare revenue summary to the finance department for recording in the city's General Ledger, incidents of missing deposit slips cause a problem in timing of recording of the deposits. The missing deposit slips add to the difficulty when performing the bank reconciliation.

Time Delay Between Bank Deposits and When Revenue is Recorded in the General Ledger

The city golf course and driving range operation collects revenues by cash and credit card. The cash revenues are deposited by the golf operations staff to the bank each day. Golf operations staff members also prepare a summary of the revenue received and submit it to the finance department for recording into the General Ledger. However, the revenue summary has not always been consistently submitted in a timely manner, causing a delay in the recording of the revenue into the city's General Ledger. This also creates an additional obstacle in reconciling the bank deposits and cash recorded in the General Ledger.

Recommendation

The City should establish procedures to address the issues above and ensure that bank statements are reconciled properly and timely.

City's Response

- **Differences Between Bank Statement and General Ledger Amounts**

The City concurs with this finding. The former accountant who was charged with the duty of bank reconciliation was consistently behind in the reconciliation, as noted in previous management letters to the City. The former accountant and former finance director did not have a handle on the outstanding check list and cash balances.

- **Timeliness**

The City concurs with this finding, as noted above.

- **Unreconciled Outstanding Checks**

The City concurs with this finding, as noted above. Additionally, once the matter of approximate \$24,000,000 of incorrect outstanding checks issued was identified, the current finance director worked with staff and Bank of the West to correct the additional two zeroes attached to the end of the checks, which prevented cancellation of the checks from being reflected on the records. The Bank of the West outstanding check list matter has been rectified and the outstanding check numbers are now properly sequenced.

- **Untimely Recording of Corrections to Payroll Checks**

The City concurs with the finding and will implement processes to ensure that payroll transactions are recorded in a timely manner.

- **Missing Deposit Slips for the City Transit Department**

The City is in the process of implementing a cash receipts module that will be used by all collection points. City staff has requested City Council approval of the acquisition of a new cash receipts module at the next regularly scheduled City Council meeting. Obtaining a new cash receipts module will enable the City to report timely and accurate cash collections. Additional procedures will be implemented to ensure that deposit slips are received by the Finance Department in a timely manner.

- **Time delay between bank deposits and when revenue is recorded in the General Ledger**

The City is in the process of implementing a cash receipts module that will be used by all collection points. Doing so, it will enable the City to report timely and accurate cash collections. Additional procedures will be implemented to ensure that deposit slips are received by the Finance Department in a timely manner.

In sum, the City concurs with Finding 4 overall, and has been taking aggressive action to address the SCO's concerns, including a proposed \$80,000 investment in a new cash receipts module.

SCO's Comment

The city concurs with the finding.

FINDING 5— Bank accounts established for the RDA were not included in that agency's financial records

One of the services the City of Montebello provides to the RDA in return for reimbursement of costs is establishing and maintaining all financial accounts, including the establishment of bank accounts. As noted in the Observation section, example 3 of our report of the Montebello RDA, dated September 22, 2011, the city failed to maintain records on two bank accounts for the RDA. In fact, RDA staff members stated that they were unaware these bank accounts existed until early 2011.

Recommendation

The city should develop and implement control procedures to ensure that all transactions are accounted for and included in the city's General ledgers.

City's Response

The City has previously responded to this matter and has taken corrective measures by recording these accounts on the general ledger of the RDA. This issue was fully resolved in a public report made to the City Council in May 2011. These amounts are reflected in the audited financial statements of RDA for FY 2009-10.

Based on the City's resolution of this matter, the SCO should eliminate this finding.

SCO's Comment

As stated in the SCO's audit report of the Montebello Redevelopment Agency, the SCO believes that the finding is necessary and appropriate as it provides additional transparency and accountability about the RDA's fiscal practices.

FINDING 6— Lack of segregation of duties

During our review of employee duties, we noted that incompatible functions are assigned to, and being performed by the accounts payable supervisor. These functions include accounts payable, payroll, and investments. Duties within these functions include performing wire transfers, performing and recording investment transactions, and generating checks for payments. Good internal controls require that these duties be segregated to avoid potential conflicts of interest and/or fraud.

Recommendation

The city should assess its current processes and implement policies and procedures to segregate incompatible functions.

City's Response

The City concurs with this finding which is reflective of past practices. In response to prior SCO audits and the new executive team's conclusions, the City has upgraded the educational requirements for these positions, requiring all candidates hold, at a minimum, an accounting degree. The City continues to assess its current processes and implement policies and procedures to segregate incompatible functions. There are three key positions that are currently vacant and being recruited for in the Finance Department. Interviews for the accountant position were completed in early December and selection of a candidate is forthcoming. Once these positions are filled comprehensive segregation of duties will occur.

The City concurs with this finding, and will ensure the segregation of incompatible functions.

SCO's Comment

The city concurs with the finding.

FINDING 7— Inadequate and outdated Administrative Policy Manual

The city's Administrative Policy Manual is not regularly updated to reflect current processes or reviewed for overall reasonableness. The city does not have a process in place to routinely review and update its Administrative Policy Manual. Therefore, documentation for completeness, accuracy, and consistency with existing processes is lacking.

This resulted in significant internal control weaknesses over the city's financial transactions and business cycles. For example:

- Procedures for processing time cards have not been updated since March 14, 1990.
- The time card procedures as stated in the manual are not reflective of actual procedures performed by the city. The city's Administrative Policy Manual, Time Card Procedure, Number VI-D-3, does not state the requirement for employees to sign their time cards; however, discussion with payroll staff members revealed that it had been a city practice to require employees' signatures on time cards except for the police, fire, and transit departments.

During our payroll testing, we noted that several time cards were not signed by the employees. Without employees' certification, the hours charged could be incorrectly stated and paid.

- The city policy manual lacks adequate documentation of the flow of accounting transactions, which contributed to accounting errors as noted in Finding 3.

Documentation provides guidance for implementing controls and serves as a basis for training new personnel in implementing them, and provides evidence the controls have operated effectively. Undocumented and outdated policies and related internal controls result in unclear roles and responsibilities and lead to improper handling of transactions. An

essential element of internal control is monitoring, which includes verification by management that policies and procedures are updated to adequately address new challenges identified by ongoing risk assessments.

Recommendation

The city should review and update its Administrative Policy Manual to ensure consistency with current processes and organizational structure, and perform periodic and ongoing reviews to ensure proper documentation, accuracy, and completeness in its financial transactions and records.

City's Response

The City staff concurs and had previously identified the need to update the Administrative Policy Manual in a presentation to the City Council and the community at the November 9, 2011 regular City Council meeting of a Management Summary Report by the Interim City Administrator and the Interim Assistant City Administrator.

The City is committed to updating its Administrative Policy Manual and ensuring that the Manual be regularly reviewed and modified to be consistent with laws, processes, procedures and the structure of the organization.

The City concurs with this finding, and has made updating its Administrative Policy Manual a priority goal, as stated in the Management Summary Report.

SCO's Comment

The city concurs with the finding.

FINDING 8— Unrestricted access to Human Resources and Payroll systems

The city provides full access to the Human Resource Management System (HRMS) and Payroll Module to staff members in Human Resources (HR) and to payroll staff members in the Finance Department. HRMS is used by the HR department for entering and maintaining employee data. The Payroll Module is used by payroll staff members to process city payroll, including entering timecard data and generating payroll checks. Staff members having full access to both HRMS and the Payroll Module system can manipulate the HR or payroll data.

Recommendation

The city should establish and implement policies to restrict access to HRMS to HR staff members and restrict access to the Payroll Module to payroll staff members.

City's Response

The City concurs with this finding and will establish and implement policies to restrict access as appropriate and ensure internal controls. The City will receive technical support from GEMS, its accounting system provider, and City executive staff will then make a determination as to which employees should have access to the Human Resources and Payroll Systems. Accordingly, the City is in the process of applying GEMS controls and programs to create enhanced security on both the Human Resources and Payroll systems.

The City concurs with this finding, and as a part of the City's ongoing execution of recommendations from the Management Systems Report and the various SCO audits, it will continue to ensure that the Human Resources and Payrolls Systems are secure.

SCO's Comment

The city concurs with the finding.

Appendix 1— Evaluation of Elements of Internal Control

		<i>Yes</i>	<i>No</i>	<i>Comments</i>
Control Environment				
A1.	Integrity and Ethical Values			
	a. Are code of conduct and other policies regarding acceptable business practices, conflicts of interest, or expected standards of ethical and moral behavior in existence and communicated to all city management and employees?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Although the city has an Administrative Policy Manual, as noted in Finding 8, the current manual is outdated and inadequate. In addition, there are instances of questionable business practices such as conflict of interest and lack of competitive bidding (Finding 1) and violation of federal tax reporting requirements (Finding 1).
	b. Does management foster, encourage, and emphasize the importance of integrity and ethical values?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	There are instances of management decisions appearing to lack integrity and ethical values. For example, as noted in Finding 1, management overrode petty cash controls and violated federal tax reporting requirements.
	c. Is every-day dealing with vendors, clients, auditors and other parties based on honesty and fairness?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Although there is a policy in place to bid expenditures costing \$50,000 or more, there are instances where the bidding process was not followed, such as engineering work performed by Infrastructure Engineering (previously AAE) (Finding 1).
	d. Does management takes action when violations of policies, procedures, or the code(s) of conduct occur?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Instances of violations of policies by low-level employees are appropriately addressed by the management; however, violations by upper management are dealt with differently as noted in Finding 1.
	e. Are instances of override of internal controls, if any, properly documented?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	During vendor payment testing, we noted proper documentation on emergency purchases; however, instances of petty cash control override were not documented or substantiated, as noted in Finding 1.
A2.	Commitment to Competence			
	a. Is management analyzing tasks relative to a particular job regarding need and extent of supervision?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Management failed to identify and analyze cause of the unreconciled cash, and delayed reconciliation as noted in Finding 4.
	b. Is management evaluating and determining the knowledge and skills needed to perform key functions?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city needs to reevaluate its hiring practices, in particular, regarding employment qualifications. The city employs staff members lacking sufficient education or experience related to job responsibility. For example, the city has a G.E.D. requirement for a supervisory position, and non-related educational experience for a key finance position. In addition, the city failed to address staff members' inability to complete timely bank reconciliations.
	c. Do employees have the competence and training necessary for their assigned level of responsibility or the nature and complexity of the entity's activities?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	It appears that finance department staff members are not properly trained to fully understand the complex financial system and city operations. Although the city offers tuition reimbursement to its staff members for continuing education, it is up to the employee to take initiative for learning new skills. As noted in Finding 3, most staff members do not have any understanding of the accounting system except as it relates to their assigned duties.
	d. Are all departments are appropriately staffed?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Some key positions currently are vacant. Insufficient staffing and significant turnover contribute to the failure to segregate duties (Finding 6); and there is inadequate review of the overall functioning of the accounting system.

Appendix 1 (continued)

		Yes	No	Comments
A3.	Management and Operating Style			
	a. Is management conservative in accepting risks, moves carefully, and proceeds only after careful evaluation?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Management made questionable decisions as noted in our RDA report and Finding 1 of this report.
	b. Is personnel turnover in key functions at an acceptable level and not excessive?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Turnover of City Administrator and key positions in the finance department contributed to the deficiencies noted in the RDA and this report.
	c. Is management's attitude positive toward internal controls and audit functions?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	As noted in Finding 7, the city's Administrative Policy Manual is inadequate and outdated. In addition, there is no adequate separation of duties due to the lack of staffing, and documents and records are inadequate to support validity of transactions, as noted in Findings 2 and 3.
	d. Are there frequent interactions of senior management and operation management in both formal and informal settings?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Certain city departments indicated that the prior Finance Director did not disseminate financial information to them. In addition, there is lack of communication among staff members within the same department.
	e. Is management's attitude appropriate toward financial reporting and other operational reporting?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city was late in filing financial transaction reports. The city's and RDA's general ledgers are inaccurate and incomplete as noted in Finding 3.
	f. Are procedures or activities in place to regularly educate and communicate to management and employees the importance of internal controls and to raise their level of understanding of controls?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	There does not appear to be a process to inform and educate regarding good internal controls practices. Also, refer to A3c.
	g. Does management give appropriate attention to internal controls and correct any known weaknesses in internal controls on a timely basis?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city has recurring uncorrected audit findings from its external auditors, such as the cash reconciliation issue. Also refer to A3c.
A4.	Organizational Structure			
	a. Is the organization structured to facilitate the flow of information throughout the entity?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city's Administrative Policy Manual includes procedures for internal and external communications; however, it appears that information is not properly communicated throughout the entity, as described by staff members.
	b. Are key managers' responsibilities adequately defined and communicated?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Department heads' responsibilities appear to be adequately defined and communicated; however, for some key staff members, it appears that their responsibilities are undefined, resulting in performance of incompatible duties as noted in Finding 6.
	c. Do managers in charge have the required knowledge, experience, and training?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Department heads within the city appear to have the required knowledge, experience, and training; however, there are some staff members in key positions who lack the required skills and knowledge to perform required duties effectively.
	d. Does the city's established reporting relationship ensure effective communication among employees, supervisors, managers, and officers?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city lacks proper communication among city departments and staff within departments.
	e. Does a process exist supporting the identification and disclosure of related-party transactions?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	We did not note a process for the identification and disclosure of related-party transactions. Note that this was also a finding by the city's external auditors. There also are citizen complaints regarding related-party transactions.

Appendix 1 (continued)

		Yes	No	Comments
A5.	Assignment of Authority and Responsibility			
	a. Is proper information considered in determining the level of authority and scope of responsibility of an employee?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Employees perform incompatible duties as noted in Finding 6.
	b. Are responsibilities for decision-making clearly linked to the assignment of authority and individuals are held accountable accordingly?	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
	c. Are employees at the right level empowered to correct problems or implement improvements?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	As noted in A4b, responsibilities of some key employees are undefined. In addition, as noted in Finding 7, the lack of adequate documentation of the city's policies and procedures results in unclear employee responsibilities.
	d. Do job descriptions exist and contain specific references to control-related responsibilities?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Job descriptions exist; however, staff members within the finance department appear to be performing incompatible duties due to employee turnover and lack of staffing.
	e. Are employees empowered to correct problems or implement improvements in their assigned processes?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Staff members in low-level positions and their immediate supervisors appear to feel uncomfortable deviating from their normal processes and, therefore, do not make any corrections or improvements to the existing process.
A6.	Human Resources Policies and Practices			
	a. Are policies and procedures established for hiring, training, and promoting employees and management, particularly in hiring and training?	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
	b. Are employees made aware of their responsibilities and expectations of them?	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
	c. Is management's response to failure to carry out assigned responsibilities appropriate?	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
Risk Assessment				
B1.	Goals and Objectives			
	a. Are there entity-wide objectives established by management?	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Citywide objectives are established and included in the city's CAFR and most recently included in the City Annual Budget.
	b. Is information relating to objectives disseminated to all city employees?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	We did not find evidence of procedural process for disseminating objectives to all city employees.
	c. Are goals (with specific targets and deadlines) established and relate to objectives?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Citywide goals relating to its objectives appear to be established; however, departmental goals are not well-defined and established, as evidenced in the inability of the finance department to reconcile its general ledgers to the bank balances.
	d. Are measurement data included in the objectives?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	We were not able to obtain any measurement data.

Appendix 1 (continued)

		<i>Yes</i>	<i>No</i>	<i>Comments</i>
	e. Is there a process in place to periodically review and update strategic plans? Is the strategic plan reviewed and approved by those charged with governance?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	We were not provided with any documentation of periodic reviews. In addition, as noted in the RDA report, the RDA budget is incomplete or missing required elements.
	f. Are managers involved in establishing objectives for which they are responsible?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Managers' involvement appears to be isolated to their departmental goals and objectives.
B2.	Risk			
	a. Does the risk-assessment process in place consider the extent and internal factors affecting objectives?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	We were not provided with any documentation for the city's risk assessment process relative to its objectives and financial reporting.
	b. Does the risk assessment process include estimating significance of risks, assessing likelihood of occurrence, and determining the needed actions to prevent risks?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	We were not provided with any information that documents that the city does, in fact, have risk assessment taking place. It appears that lack of risk assessment contributed to the current financial crisis of the city.
	c. Is management considering the risks related to Human Resources, budgeting, labor relations, and Information Systems?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	As noted in Finding 8, due to the nature of the financial system used by the city, full access to Human Resources Management System (HRMS) is made available to payroll staff members in the finance department, posing risk of manipulation of HR information by unauthorized individual.
	d. Are risks related to the ability of an employee to initiate and process unauthorized transactions appropriately identified?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Refer to B2c.
	e. When risks are identified, are existing controls examined to determine whether there has been a failure in controls, and was action been taken to address them?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Refer to B2b.
	f. Is fraud assessment an integral part of the risk identification process?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Refer to B2b.
	g. Does the entity's assessment of fraud risk consider incentives and pressures, attitudes, and rationalizations as well as the opportunity to commit fraud?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Refer to B2b.
	h. Does management identify all significant relationships including service providers, suppliers, citizen groups, creditors, etc.?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Refer to A4e.

Appendix 1 (continued)

		Yes	No	Comments
B3.	Managing Change			
	a. Are there mechanisms in place to anticipate, identify, and react to routine events or acts that affect achievement of objectives?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	There does not appear to be a mechanism in place to identify and manage change affecting the city. The failure to manage change may be one of the contributing factors to the current financial crisis faced by the city.
	b. Are there mechanisms in place to identify and react to changes that can have dramatic and pervasive effect on the city?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	See B3a.
	c. Does the governing body adopt a budget for all funds in accordance with state statutory or other requirements?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Refer to the RDA report, Finding 11.
	d. Is there a process in place to ensure that the accounting department and those charged with governance are sufficiently aware of significant related party transactions to ensure they are appropriately accounted for and disclosed?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Refer to A4e.
Control Activities				
C1.	Management Reviews			
	a. Are administrative and operation policies for each of the entity's activities in writing and do they set clear procedures for compliance?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city lacks complete written policies and procedures for its transaction cycles and operations.
	c. Are controls performed to check for reasonableness, allowability, and validity of transactions?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	As noted in Finding 3, numerous Journal Voucher (JV) transactions lack proper notation and supporting documentation. Although these JVs contained evidence of proper review and approval, it appears they were performed as a process instead of as a control. These JVs should have contained sufficient information and supporting documentation prior to approval for processing.
	b. Are control activities regularly evaluated to ensure they are still appropriate and working as intended?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	As noted in Finding 7, the city's Administrative Policy and Procedures Manual is inadequate and outdated.
	c. Does management compare different sets of data and investigate variances?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	As noted in Finding 4, the city is unable to reconcile its cash recorded on the general ledger to cash per the bank statement.
	d. Are duties properly segregated?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	As noted in Finding 6, certain incompatible functions are not properly segregated.

Appendix 1 (continued)

		<i>Yes</i>	<i>No</i>	<i>Comments</i>
Information and Communication				
D1.	Information			
	a. Are mechanisms in place to obtain relevant information on program, legislative or regulatory developments, budget, or economic changes?	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
	b. Have long range information technology plans been developed and linked with strategic initiatives?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city implemented a new financial system in 2007; however, as noted in Finding 3, due to staff turnover within the finance department, no one within the department currently has complete knowledge on the flow of transactions as a whole. In addition, it appears the city needs to improve access restriction to the system as noted in Finding 8.
	c. Are process procedures sufficiently formal such that management can determine whether the control objective is met, documentation supporting the procedures is in place, and personnel routinely know the procedures that need to be performed?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	We could not find a process in place. The city also lacks adequate internal controls documentation.
	d. Is data underlying financial statements captured completely, accurately, and timely, in accordance with the entity's policies and procedures and in compliance with laws and regulations?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city's financial reports are late, inaccurate, and incomplete.
D2.	Communications			
	a. Are communication vehicles sufficient in effecting communications?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Refer to A4a.
	b. Do employees know the objectives of their own activity and how their duties contribute to achieving objectives and others goals?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Employees appear to know the objectives of their own activities. However, it does not appear that this knowledge extends to other staff members' objectives and goals, and overall objectives of the city.
	c. Are communications channels in place for people to report suspected activity and is appropriate feedback provided?	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Citizen complaint policy is included in the city's Administrative Policy Manual.
	d. Does adequate communication exist across the organization? Is information complete, timely, and sufficient?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	There is lack of communication within the city.
	e. Are feedback mechanism for external parties (suggestions, input, complaints) directed to relevant internal parties?	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
	f. Does management make certain that the advice and recommendations of oversight agencies and other auditors are fully considered and take action to correct any problems and weaknesses they identify?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city has not addressed several of the external auditor's repeated findings including untimely cash reconciliation, adequate segregation of duties, and timely passage of city budget.

Appendix 1 (continued)

		Yes	No	Comments
Monitoring				
E1.	Ongoing Monitoring			
	a. Are operating reports integrated or reconciled with financial and budgetary reporting system data?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Our inquiry with city departments revealed that departmental operating reports are not reconciled with the financial data. In addition, there is low reliance on the data generated by the accounting system due to its complexity, and untimely recording of transactions, as noted in Finding 3.
	b. Are operation personnel required to “sign off” on the accuracy of their unit’s records?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The “sign-off” on the accuracy of records appears to be more of a process rather than a control.
	c. Are communications with outside parties and monthly statements of accounts payable used as a control monitoring technique?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	From our inquiry and observations, it appears that city staff members do not use inquiry and questions of external parties as a monitoring technique.
	d. Are periodic comparisons of amounts recorded by accounting system compared with physical assets?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city contracts with an outside party to maintain its physical assets listing. As noted by the external auditor on its Schedule of Findings for FY ended June 30, 2010, the listing maintained by the outside party did not agree to the city’s general ledger due to the delay with the city providing asset additions to them.
	e. Does a policy exist to adopt an Incompatible Activities Statement of Conduct?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	The city’s current Administrative Policy Manual does not contain a policy regarding incompatible activities.
E2.	Separate Evaluation			
	a. Do employees with appropriate skills evaluate portions of the internal control?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	From our inquiry, there appeared to be no evaluation of internal controls by staff and management.
	b. Do city staff members gain sufficient understanding of internal controls?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Procedure for monitoring of internal controls is not included in the City’s Administrative Policy Manual and from our inquiry, has not been performed by city staff.
	c. Are policy manuals, organization charts, and operational instructions available for review?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	City Administrative Policy Manual, Departmental policies, and organization charts were available for review. However, as noted in Finding 7, the City’s Administrative Policy manual is inadequate and outdated.
E3.	Reporting Deficiencies			
	a. Do means of obtaining reports of deficiencies from both internal and external sources exist?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Internal report of deficiencies is not maintained, while report of deficiencies from external auditors can be found on audit reports issued. The city, however, did not make available, the Findings portion of the current audit report on the copy that was posted online.
	b. Is there ongoing monitoring of internal controls?	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Refer to E2b.
	c. Are the transactions or events identified investigated, causes determined, and problem corrected.	<input type="checkbox"/>	<input checked="" type="checkbox"/>	While issues such as delayed cash reconciliation and other deficiencies are identified, these problems are not corrected by the city staff in a timely manner.
	d. Reports from external sources (e.g., external auditors, regulators) are considered for their internal controls implications, and timely corrective actions are identified and taken.	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Audit findings from external auditors are not corrected in a timely manner.

**Attachment—
City's Response to
Draft Audit Report**

December 9, 2011

Mr. Jeffrey V. Brownfield
Chief, Audit Division
California State Controller's Office
P.O. Box 942850
Sacramento, CA 94250-5874

Dear Mr. Brownfield:

The City of Montebello ("City") received the draft State Controller Review Report for its State and Federal Expenditures dated November 2011, via e-mail on November 29, 2011 ("Draft Review Report"). Per our discussion, the City's response is due on Friday, December 9, 2011, and is transmitted herewith.

As noted in the City's prior letter to you, the City respectfully requests the State Controller carefully review and consider the City's responses before issuing the final Review Report. The City has made significant efforts to address the concerns raised by the SCO, and is in the process of updating its internal processes and policies. You will note that for a majority of the findings, the City acknowledges and accepts the SCO's findings as stated, and will ensure that certain past practices will not be repeated.

As you are aware, the City is under new administration that the City Council specifically selected to guide the City through its current financial difficulties. Since the new administration was installed in May 2011, the City has taken numerous steps to address the City's financial difficulties. For instance, in November 2011, the new administration oversaw and completed the sale of a \$2.5 million Tax and Revenue Anticipation Note ("TRAN") to ensure the City's continued financial solvency. The closing coincided with the TRAN's MIG2 rating from Moody's Investors Service on October 21. Moody's noted 2011 improvements to the City's General Fund balance sheet, as well as the City's favorable projections for the General Fund closing cash balance for June 30, 2012. In addition, the administration recently presented a clear plan, the "Management Summary Report," which outlined further steps for the City's long-term economic stability. (Attached to the Response as **Exhibit A.**) Further, last week the City received notice from Standard & Poor's affirming the Montebello Redevelopment Agency's "A-" rating, and removing the Agency from Credit Watch.

The City's responses to the findings in the Draft Review Report are attached. As we have discussed in the past, the City and its Redevelopment Agency are fully committed to meeting all existing statutory and regulatory requirements. The City appreciates the efforts of the State Controller's office in helping the City and Agency identify issues that need to be addressed, so that we can meet our common goals of ensuring a successful financial future for the City and Agency.

Jeffrey V. Brownfield
California State Controller's Office
December 9, 2011
Page 2

The City looks forward to the receipt of your final report reflecting the information provided in our responses.

Sincerely yours,

Larry Kosmont
Interim City Administrator

Enclosures: City's Response to Draft Review Report
 Ex. A. Management Summary Report (dated December 9, 2011)

cc: Keith Breskin, Interim Assistant City Administrator
 Francesca Tucker-Schuyler, Director of Finance

CITY OF MONTEBELLO
RESPONSE TO DRAFT REVIEW REPORT, ADMINISTRATIVE AND INTERNAL
ACCOUNTING CONTROLS
(July 1, 2009 through June 30, 2010)

Finding 1: Problems with personnel transactions and expenditure approvals.

- **City actions may have increased the former City Administrator's pension above the level it should have been and this may constitute pension-spiking**

City response: A review of City files confirms that a prior City Council executed a separation agreement on November 2, 2007, to terminate the employment of a former City Administrator and that former City staff failed to properly process the termination. When current City executive staff learned of this issue in 2011, City staff immediately began working with CalPERS to correct deficiently-reported earnings to CalPERS from the period the prior City Administrator was terminated to when he was rehired by the City on January 16, 2008. Subsequently a Notice of Change was sent to the City to reverse payroll for the applicable period of time. City Payroll staff have taken steps to make the corrected reversal, and have been in contact with CalPERS to accommodate the reversal which has been delayed due to CalPERS' current systems upgrade.

To ensure that this issue is avoided in the future, City executive staff will recommend a Personnel Procedure to be adopted by the City Council, which will provide for a written communication process as applicable to changes in the employment status with employees, including, but not limited to, the City Administrator, so that those changes can be properly processed in a timely manner.

- **Violation of Tax Reporting Requirements**

City response: The City concurs with this finding, and remains fully committed to complying with federal and state tax reporting requirements and utilizing the proper reporting forms. The City will ensure that future bonuses as well as ongoing stipends are reported as required. The City will contact the appropriate taxing agencies to correct any errors with previous reporting as deemed necessary.

//
//
//

**CITY OF MONTEBELLO RESPONSE TO DRAFT REVIEW REPORT,
ADMINISTRATIVE AND INTERNAL ACCOUNTING CONTROLS**
December 9, 2011

- **Inappropriate Treatment of Severance Pay**

City response: The City acknowledges that on July 18, 2006, the City and the former Director of Community Development entered into a separation agreement to include severance and other benefits. Further, on January 4, 2008, CalPERS sent the City a letter indicating that the compensation reported from July 2006 to June 2007 was final settlement pay and should not have been reportable to CalPERS as compensation earnable. Although this issue was not corrected at that time, current City executive staff promptly reversed the transaction on June 13, 2011 when it was first brought to their attention. As such, all applicable erroneously-reported compensation has been corrected with CalPERS.

To avoid this issue in the future, City executive staff will work closely together to correct any reporting errors with CalPERS in a timely manner. City executive staff will recommend a Personnel Procedure to be adopted by the City Council, which will provide for a written communication process as applicable to changes in the employment status with employees, including, but not limited to, the City Administrator, so that those changes can be properly processed in a timely manner. In the Interim City Administrator's recent Management Summary Report, which was presented to the City Council on November 9, 2011, the Interim City Administrator's recommendation was to improve internal operating systems.

- **Override of Petty Cash Controls**

City response: The City concurs with this finding and will ensure that policies and procedures related to petty cash controls are updated and enforced consistently.

- **Conflict of Interest and Lack of Competitive Bidding for Engineering Contract and Projects**

City response: The City acknowledges this finding, and is currently in the process of re-evaluating its current agreement for engineering services. In the Interim City Administrator's recent Management Summary Report, which was presented to the City Council on November 9, 2011, the Interim City Administrator's recommendation was to bid the contract after consulting an external engineering expert to review the existing practices and make recommendations. A copy of the updated Management Summary Report is attached as **Exhibit A**. In fact, the City recently issued a Request for Proposals for such an expert to review the current engineering processes and the agreement for engineering services. It is anticipated that the expert, once retained, will complete its analysis by February 2012.

**CITY OF MONTEBELLO RESPONSE TO DRAFT REVIEW REPORT,
ADMINISTRATIVE AND INTERNAL ACCOUNTING CONTROLS**
December 9, 2011

As noted by the SCO, this finding regarding the City's award of the engineering services contract to Advanced Applied Engineering, Inc. ("AAE") was previously identified in the review report of state and federal expenditures. In response to that report, the City provided a lengthy rebuttal to the SCO's findings. The City expressly informed the SCO that to apply a later-adopted ordinance *to the terms* of an existing contract, potentially placed the City in unnecessary jeopardy. In particular, the automatic extension provision of the contract *was part of the contract* that was awarded in January 2005, *two years prior* to the adoption by the City Council of Ordinance No. 2304, which established Chapter 3.21 ("Contracts for Professional and Special Services") of the Montebello Municipal Code ("MMC"). Chapter 3.21 does not expressly apply retroactively, and if the City took the position that Chapter 3.21 applied to the automatic extension provision of the contract (without any express intent in the ordinance itself), it is possible the City may be subject to a claim that it breached the agreement, or that the law itself impaired the obligations of a contract.

It appears to the City that the better solution is to follow the process City staff has already initiated, which is to select an engineering expert to provide recommendations, and then subsequently improve engineering and public works procedures by adopting a competitive bid process as directed by a thorough analysis of an independent expert. Although the City maintains its position that the MMC Chapter 3.21 does not apply to the terms of the engineering services contract, the City acknowledges the fact that certain engineering projects that exceeded \$50,000 and that arose after the implementation of Chapter 3.21 should have been competitively bid. The City is committed to receiving the best competitive prices for its capital improvement projects, has taken affirmative steps in evaluating the current agreement with AAE, and will be making recommendations to overall engineering processes as well as going out to bid for its engineering services before the end of the current fiscal year.

In summary, the City acknowledges and concurs with the majority of Finding 1, has taken affirmative steps to addressing the various issues raised therein, and will ensure that its policies and procedures are both updated and enforced.

Finding 2: Cash impairment in the City's investment pool.

City response: The City has responded, previously, to the matter of cash impairment in response to prior SCO reports. The matter of the use of restricted funds was corrected by the City in February of 2011. The City can document that there was no cash impairment since the City's

**CITY OF MONTEBELLO RESPONSE TO DRAFT REVIEW REPORT,
ADMINISTRATIVE AND INTERNAL ACCOUNTING CONTROLS**
December 9, 2011

investment portfolio indicates that it exceeded the cash balances which are deemed restricted. Additionally, as of March 2011, the monthly investment reports submitted to the Council and the City's Investment Committee includes a balance that separates the general fund balance of the pooled cash from that of the restricted funds.

The City's accounting system records deposits and disbursements by fund. Therefore the cash balances for each specific fund is available. Please see response to Finding 3 for additional comments.

There was no cash impairment; therefore, the SCO should eliminate this finding.

Finding 3: Questions about the accuracy, reliability and timeliness of the data in the City's accounting system.

City response: The general ledger balances produced by Government e-Management Solutions, Inc. (GEMS), the City's accounting system, can be relied upon, if the information posted is correct. It has recently been determined that the information posted into the accounting system in July 2008 and July 2009, by the former finance director and former accountant was incorrect. Ending balances of June 30, 2008 were duplicated via journal entry for all balance sheet accounts, for all funds, in July 2008, which overstated assets, liabilities and fund balances. Ending balances of June 30, 2009 were duplicated, again, via journal entry for all balance sheet accounts, for all funds, further corrupting the integrity of the financial data in the City's general ledger. Ad hoc reporting systems were used to generate the trial balance report to compensate for the incorrect balances of the general ledger.

Upon discovery of the duplicated entries, corrective actions were taken to reverse the duplications and to provide the current auditors with a correct general ledger that can be relied upon to conduct the annual audit.

- **Implementation of a New Accounting System**

City response: Although the City concurs that there has been recent staff turnover in the Finance Department, such turnover is not the reason for the improper use and implementation of the new accounting software. The new software was implemented in July of 2007 and staff turnover did not occur until Fiscal Year 2010-11. Once the software was implemented, the former finance director and the former accountant had the responsibility to ensure that there was proper

**CITY OF MONTEBELLO RESPONSE TO DRAFT REVIEW REPORT,
ADMINISTRATIVE AND INTERNAL ACCOUNTING CONTROLS**
December 9, 2011

documentation to support the balances as represented in the general ledger. It has become apparent that the system was not set up properly from the onset and errors were made in transactions, as noted above.

Moreover, based on the various prior SCO's audits, as well the Management Systems Report from Kosmont Companies (the City's independent consulting firm that has provided Interim City management and financial turnaround services), the City acknowledges its need to implement a better accounting structure. Specifically, an improved Accounting System was listed as the first "Wish-List" item in the Interim City Administrator's updated Management Summary Report (attached as **Exhibit A**). The City agrees that a specific accounting module must be identified, and that personnel must be trained on using the module.

- **Inadequate Documentation of Overall Accounting Procedures and Processes**

City response: Documentation of the overall procedures and processes of the accounting system does exist. The City acknowledges that a climate existed whereby staff's understanding in the overall procedures and processes was limited. The City will examine and evaluate methodologies to increase understanding and participation.

- **Delays in Closing of Financial Records**

City response: The City acknowledges that it did not close its FY 2009-10 financial records within six months after year end. The audit for FY 2009-10 was delayed due to various issues including incorrect and insufficient documentation provided by the former finance director and former accountant to the auditors. Once the audit was completed, in June 2011, the current finance director closed the books.

- **Delayed Adoption of a Budget**

City response: The City concurs with this factor. To correct this deficiency, the first order of business of current Interim City Administrator Larry Kosmont was to obtain formal adoption of the FY 2010-11 budget by the City Council, which took place in June 2011, six weeks after Kosmont Companies initiated its assignment as Interim City Administrator.

//

//

**CITY OF MONTEBELLO RESPONSE TO DRAFT REVIEW REPORT,
ADMINISTRATIVE AND INTERNAL ACCOUNTING CONTROLS**
December 9, 2011

- **Insufficient Information Supporting Journal Vouchers**

City response: The City concurs with this observation. The former accountant, historically, did not provide sufficient documentation and detail to the various journal entries prepared. It appears that in prior years, the former Finance Director did not require or enforce sufficient documentation as he signed off on many of these journal entries. The entries prepared by the former finance director did not have adequate documentation as well. This further delayed of the FY 2009-10 audit and the closing of the books.

In sum, the City concurs with a majority of the “factors” in Finding 3, and has taken corrective actions to address many of the issues raised therein. However, the City disputes that the documentation of the overall procedures and processes of the accounting system is inadequate.

Finding 4: Significant problems with the City’s cash reconciliation process.

- **Differences Between Bank Statement and General Ledger Amounts**

City response: The City concurs with this finding. The former accountant who was charged with the duty of bank reconciliation was consistently behind in the reconciliation, as noted in previous management letters to the City. The former accountant and former finance director did not have a handle on the outstanding check list and cash balances.

- **Timeliness**

City response: The City concurs with this finding, as noted above.

- **Unreconciled Outstanding Checks**

City response: The City concurs with this finding, as noted above. Additionally, once the matter of approximate \$24,000,000 of incorrect outstanding checks issued was identified, the current finance director worked with staff and Bank of the West to correct the additional two zeroes attached to the end of the checks, which prevented cancellation of the checks from being reflected on the records. The Bank of the West outstanding check list matter has been rectified and the outstanding check numbers are now properly sequenced.

**CITY OF MONTEBELLO RESPONSE TO DRAFT REVIEW REPORT,
ADMINISTRATIVE AND INTERNAL ACCOUNTING CONTROLS**
December 9, 2011

- **Untimely Recording of Corrections to Payroll Checks**

City response: The City concurs with the finding and will implement processes to ensure that payroll transactions are recorded in a timely manner.

- **Missing Deposit Slips for the City Transit Department**

City response: The City is in the process of implementing a cash receipts module that will be used by all collection points. City staff has requested City Council approval of the acquisition of a new cash receipts module at the next regularly scheduled City Council meeting. Obtaining a new cash receipts module will enable the City to report timely and accurate cash collections. Additional procedures will be implemented to ensure that deposit slips are received by the Finance Department in a timely manner.

- **Time delay between bank deposits and when revenue is recorded in the General Ledger**

City response: The City is in the process of implementing a cash receipts module that will be used by all collection points. Doing so, it will enable the City to report timely and accurate cash collections. Additional procedures will be implemented to ensure that deposit slips are received by the Finance Department in a timely manner.

In sum, the City concurs with Finding 4 overall, and has been taking aggressive action to address the SCO's concerns, including a proposed \$80,000 investment in a new cash receipts module.

Finding 5: Bank Accounts established for the RDA were not included in that agency's financial records.

City response: The City has previously responded to this matter and has taken corrective measures by recording these accounts on the general ledger of the RDA. This issue was fully resolved in a public report made to the City Council in May 2011. These amounts are reflected in the audited financial statements of RDA for FY 2009-10.

Based on the City's resolution of this matter, the SCO should eliminate this finding.

**CITY OF MONTEBELLO RESPONSE TO DRAFT REVIEW REPORT,
ADMINISTRATIVE AND INTERNAL ACCOUNTING CONTROLS**
December 9, 2011

Finding 6: Lack of segregation of duties.

City response: The City concurs with this finding which is reflective of past practices. In response to prior SCO audits and the new executive team's conclusions, the City has upgraded the educational requirements for these positions, requiring all candidates hold, at a minimum, an accounting degree. The City continues to assess its current processes and implement policies and procedures to segregate incompatible functions. There are three key positions that are currently vacant and being recruited for in the Finance Department. Interviews for the accountant position were completed in early December and selection of a candidate is forthcoming. Once these positions are filled comprehensive segregation of duties will occur.

The City concurs with this finding, and will ensure the segregation of incompatible functions.

Finding 7: Inadequate and outdated Administrative Policy Manual.

City response: The City staff concurs and had previously identified the need to update the Administrative Policy Manual in a presentation to the City Council and the community at the November 9, 2011 regular City Council meeting of a Management Summary Report by the Interim City Administrator and the Interim Assistant City Administrator.

The City is committed to updating its Administrative Policy Manual and ensuring that the Manual be regularly reviewed and modified to be consistent with laws, processes, procedures and the structure of the organization.

The City concurs with this finding, and has made updating its Administrative Policy Manual a priority goal, as stated in the Management Summary Report.

Finding 8: Unrestricted access to Human Resources and Payroll Systems.

City response: The City concurs with this finding and will establish and implement policies to restrict access as appropriate and ensure internal controls. The City will receive technical support from GEMS, its accounting system provider, and City executive staff will then make a determination as to which employees should have access to the Human Resources and Payroll Systems. Accordingly, the City is in the process of applying GEMS controls and programs to create enhanced security on both the Human Resources and Payroll systems.

**CITY OF MONTEBELLO RESPONSE TO DRAFT REVIEW REPORT,
ADMINISTRATIVE AND INTERNAL ACCOUNTING CONTROLS**
December 9, 2011

The City concurs with this finding, and as a part of the City's ongoing execution of recommendations from the Management Systems Report and the various SCO audits, it will continue to ensure that the Human Resources and Payrolls Systems are secure.



City of Montebello *Management Summary Report*

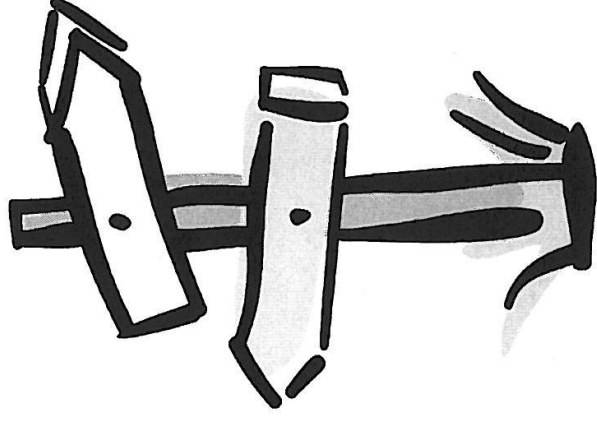
**Originally Presented November 9, 2011 by:
*Kosmont Companies, Interim City Administrator***

Updated: December 9, 2011

Report Outline



- **Progress Update on Financial Recovery**
- **The Continued Road to Recovery**
- **Montebello's Future: Next Steps for Success**



Progress Update on Financial Recovery



Context at Kosmont's Assignment Initiation: A Tough Time to be in a Tough Spot



- **When the music stopped, Montebello was caught without a safe harbor:**
 - Most severe recession in modern history
 - Spent its reserves (no rainy day account)
 - Inadequate and outdated accounting systems and records
 - Council recalls and Administrator vacancies/turnover
 - Hostile credit environment due to financial markets dysfunction
 - Media attention negative due to "looking for the next Bell" mentality
- **These circumstances (among others) made Council action on the Financial Turnaround imperative**
- **Turnaround plan began May 12 when Kosmont Companies installed as City Administrator/Turnaround Specialist and First Southwest as Fin. Advisor**
- **Kosmont was retained to provide Interim City Administrator services while engineering short-term financial turnaround**
- **Agreement extended to December 31, 2011**

Financial Distress Unfolded in Early 2011



sgvtribune.com
SAN GABRIEL VALLEY

Whittier Daily News
WHITTIER, CALIFORNIA

Los Angeles Times

Date	Headline
Feb 19:	Fiscal Mess Fuels Crisis in Montebello
Feb 22:	D.A.'s Office opens inquiry into off-the-books bank accounts in Montebello
Feb 24:	Montebello Seeks Missing Bank Accounts
Mar 10:	Solution nears in mystery of off-the-books \$1 million account in Montebello
Mar 31:	Montebello May Have Trouble Making Payroll, Paying Bills
Apr 22:	California Orders Audit of Montebello Finances
Apr 22:	Montebello officials consult bankruptcy attorneys
Apr 23:	Montebello May Face Insolvency if it Doesn't Close Budget Deficit
Apr 28:	Federal housing department freezes Montebello funds
Apr 28:	Montebello to subpoena suspect bank records; HUD suspends funding to city because of violations
Apr 29:	Public corruption prosecutors launch criminal investigation of Montebello bank accounts
May 5:	Troubled Montebello's Bonds Downgraded to Junk Status
May 14:	Special Report: Montebello uses financial maneuver to help repay \$17M loan from its redevelopment agency
Jun 19:	HUD auditing Montebello over use of federal dollars
Jun 30:	FBI is Investigating Montebello's Finances

Kosmont Companies Approach to the Interim City Administrator Assignment



- Primary focus was to review the City's financial condition on an expedited basis and to generate a responsive an effective short term turnaround while laying the base for long term recovery

Weeks ~ 1 through 6 (Mid-May through June)	Weeks ~ 7 through 23 (July through October)	Weeks ~ 24+ (November onward)
<ul style="list-style-type: none"> • Focus on understanding and stabilizing cash flow (rev. & exp.) • Moving toward a balanced budget pegged to previous year cash flow • Manage cash flow based on available General Fund ("GF") reserves that had not been spent (e.g. insurance & water) • Draft 5-Yr Financial Recovery Plan • Focus on <i>immediate</i> financial turnaround 	<ul style="list-style-type: none"> • Initiate systemic overhaul of financial system • Concurrently observe and determine other necessary organizational "fixes" (<u>while preserving employee base</u>) • Work through various audits <ul style="list-style-type: none"> ➢ State Controller (4 of 4) ➢ HUD ➢ Transportation ("FTA") ➢ Bond Insurer • Initiate short-term borrowing ("TRAN") efforts • Improving City's credit rating with Moody's and S&P • Generate <i>positive media exposure</i> 	<ul style="list-style-type: none"> • Provide Management Summary Report as summary of observations and recommendations • Offer direction for ongoing financial management improvements and <u>organizational enhancements (while restoring employee compensation to competitive levels)</u> • Prescription for implementation for new City Administration • Kosmont agreement extended to December 31, 2011 • <i>Key objective is to adhere to 5-Year Financial Recovery Plan ("FRP" or "The Plan")</i>

Financial Recovery:

What's Been Accomplished



- ✓ Adopted 5-Year Financial Recovery Plan (“FRP”), including balanced 2011/12 budget (w/ \$1 million in reserves) and Guiding Financial Principles
- ✓ Corrected inappropriate past practices and implementing new procedures
- ✓ Successfully dealing with numerous identified “Buckets of Peril”:
 - Various audits (e.g. HUD, Bond Insurer, State Controller, FTA)
 - Evaluated Redevelopment Legislation, filed recommended continuation of redevelopment in Montebello, filed appeal to reduce annual payment to the State
 - \$1.24 million reduction approved = more RDA funds for City Economic Dev. Efforts
- ✓ Continued execution on “Buckets of Opportunity” (e.g. user fee updates, Costco, oil extraction, economic development projects):
- ✓ Retained firm to assist in the pursuit of grant opportunities
- ✓ Short term cash flow financing (TRAN)
 - Obtained investment-grade credit rating (Moody’s – MIG 2)
 - Negative outlook removed from City as an issuer (revised to “neutral”) by Moody’s and downgrade warning lifted from Redevelopment Agency by Standard and Poor’s (“S&P”)
 - Closed \$2.5M TRAN on Thursday November 10, 2011 at 4.85%

Seven Audits in Six Months



June 2011

Bond Insurer Audit

Sept - Nov 2011

SCO Audits (4 of 4)

April 2011

FTA Audit

June 2011

HUD Audit

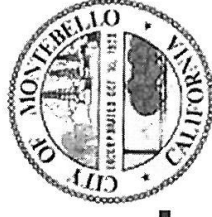
1. RDA

2. Gas Tax

3. Fed/State Exp.

4. Internal Controls

Overview of Various Audits – All Audits Focus on Past Years and Practices (2005 to 2010)



Audit	When Received	Outcome	Next Steps
Federal Transportation Administration ("FTA")	April 2011	<ul style="list-style-type: none"> Concerns about City's overall financial condition and Transportation Department systems and controls Initial response issued by City on June 15, 2011 Revised and final response issued on July 21, 2011, including update on financial turnaround and extensive list of actions being taken to address concerns (e.g. appropriation of funds for emergency generator for City information technology center) 	<ul style="list-style-type: none"> City Administration is committed to full compliance with all FTA requirements on an on-going basis
Bond Insurer – National Public Finance Guarantee ("NPF")	June 2011	<ul style="list-style-type: none"> Response to negative media (e.g. bank accounts) Proactive meeting and follow-up – No further action 	<ul style="list-style-type: none"> Continued follow-up as appropriate
Department of Housing & Urban Development ("HUD")	June 2011	<ul style="list-style-type: none"> 31 "Findings" and 2 "Concerns" regarding the management and oversight of the CDBG and HOME programs by the City City submitted corrective Action Plan, completed 13 corrective actions, completed \$2.6 million in repayments 	<ul style="list-style-type: none"> City Staff will continue to execute corrective Action Plan City will collaborate with HUD-provided technical assistance Status and go-forward process meeting scheduled

Overview of Various Audits – All Audits Focus on Past Years and Practices (2005 to 2010)



Audit	When Received	Outcome	Next Steps
State Controller Office ("SCO"): 1. RDA 2. Gas Tax 3. Fed & State Exp. 4. Internal Controls	1. RDA: Final Report Received Sept. 2011 2. Gas Tax: Final Report Received Oct 2011 3. Fed & State Exp.: Draft Report Received Oct 2011 4. Internal Controls: Draft Report Received Nov 2011	<ul style="list-style-type: none"> Certain practices of Agency are not acceptable and need correction (e.g. expenditure policies regarding conferences, networking, related items) Montebello's new management team has consistently acknowledged the need to make comprehensive financial and accounting improvements, and is in process of implementing City experts (Auditors & RDA CPA specialists, City Attorney) disagree with certain findings RDA Audit does not materially affect the Gen. Fund Gas Tax Account was not impaired (accounting process revised) Fed & State Funds Report discussed "unsupportable admin costs" (addressed by cost allocation model update in progress), ineligible Transit Fund costs (reimbursed), Transit Fund cash impairment (changes to accounting practices initiated to correct appearance of impairment), and an engineering services contract issue (recommendation to bid contract and consult external engineering expert) Administrative and Internal Accounting Controls report received 11/29/11 – Comments in progress RDA Audit and SCO's press release included misleading data, which resulted in headlines that were received negatively by the financial community 	<ul style="list-style-type: none"> City Staff will implement major findings when all audit reports are received and concluded (e.g. major contracts and service agreements will be competitively bid and reviewed) Some findings have been corrected (e.g. funds reimbursed for Transit Fund costs)

Status of Grant Opportunities



Grant	Purpose	Amount	Status
HUD Disaster Recovery Initiative	Update Safety Element of General Plan, including Local Hazard Mitigation Plan	\$250,000	Pending - Submitted 9/14/11
Cal Recycle Tire Derived Product	Replace sand and woodchips with 100% recycled rubber mulch at multiple playgrounds in Public Parks	\$150,000	Pending - Submitted 9/28/11
U.S. Soccer Foundation	Build or upgrade fields, provide player and team equipment, or provide sports lighting or irrigation	\$15,000 - \$200,000	Due 11/18/11
EPA Brownfields Grants	Address sites contaminated by petroleum and hazardous substances, pollutants, or contaminants	<ul style="list-style-type: none"> Assessment Grants: Up to \$200,000 each Revolving Loan Fund: Up to \$1 million each Cleanup Grants: Up to \$200,000 each 	Due 11/28/11
Hearst Foundation Grants	Assist organizations in the fields of education, health, culture and social service (e.g. higher education, hospitals, after-school programs, family support, job training programs)	\$2,000 - \$500,000+	Due ASAP
Baseball Tomorrow Fund	Maintenance of baseball fields (e.g. lighting, fencing)	Average award: \$39,000	Due ASAP



Update on Short Term Borrowing (TRAN)

Moody's and S&P Credit Update



- TRAN obtained investment-grade credit rating (Moody's – MIG 2)
- Negative outlook removed from City as an issuer (revised to “neutral”) by Moody's and downgrade warning lifted from Redevelopment Agency by Standard and Poor's (“S&P”)
- Positive rating supports improved credit for Montebello, which was one of the FRP's objectives
- Meant to reflect current financial position and prospect for improvement in the near-term, including level of reserves, financial flexibility and ability to absorb additional budgetary pressure

➤ *Affirms progress of Financial Recovery*

Financial Recovery Plan – At the Crossroads



<u>Date</u>	<u>Activity</u>
Aug. 24	City Council approves TRANs financing
Sept. 8	As Placement Agent, De La Rosa (DLR) distributes Private Placement Memorandum to potential investors; DLR salespeople provided talking points
Sept. 14	DLR had spoken to about 20 mutual funds and confident that TRANs will be closed by end of September
Sept. 15	State of CA sells \$5.4 billion of RANs maturing in May/June 2012 at yields 0.38% to 0.40% (rated MIG1/SP1+/F1)
Sept. 21	DLR communicates challenges due to investor return relative to investor resources necessary to review the credit (small size with significant “media noise”)
Sept. 22	“\$31 Million” Headline coverage of SCO media release regarding RDA/Gas Tax Audit
Sept. 26	Final discussions with two potential investors but credit concerns and “media noise” are cited by these investors
Oct. 15	City initiates “Plan B” – pursuit of short-term credit rating
Oct. 21	Moody’s assigned MIG 2 credit rating to TRAN, removes negative outlook from City as Issuer – Investor conversations continue
Nov. 10	TRAN closed at 4.85% with institutional investors (\$2.5 million)

TRAN Terms (Closed 11/10/11)



Tax & Revenue Anticipation Notes (TRANS)		Terms
Par Amount	\$2,500,000	
Interest Rate	4.85%	
Financing Costs ^{1,2}	\$160,000	
Interest Costs	\$74,434	
Closing Date	November 10, 2011	
Maturity Date	June 21, 2012	
Placement Agent	Citigroup	
Investor	Oppenheimer Funds	

¹ Figures approximate, subject to change

² Financing costs include fees to Note Counsel, Financial Advisor, Placement Agent, Placement Agent's Counsel, Paying Agent, Rating Agency, CUSIP Number

Management & Operational Consequences TRANS vs. Internal Borrowing



- With a TRAN in place (Plan A), City now operates on a productive and strategic basis. Ability to execute on key economic development / redevelopment projects in timely pursuit of the 5-year Financial Recovery Plan ("FRP").
- TRAN placement enables the City to avoid management and operational focus on streamlining and deferring costs, which is time consuming and dilutes recovery efforts
- Focus now on resolving audit findings, issues, and compliance and preparing for the February Mid-Year Financial Review

Summary of Recovery Progress



- Adopted 5-Year Financial Recovery Plan (“FRP”), including balanced 2011/12 budget (w/ \$1 million in reserves) and Guiding Financial Principles
- Cash Flow management efforts have worked – improved from an approximately \$2 million shortfall hitting in October to an approximate \$500,000 in late November / early December with later year shortfalls at approximately \$1.3 million (which can be further reduced)
- **No loss of employees or payroll risk** from this point (despite errant news reports)
- Achieving financing was challenging due to the overwhelming amount of concurrent financial work (budgets, TRAN marketing and negotiation, State Redevelopment legislation, audits)
 - **Seven (7) audits within 6-month timeframe**
 - FTA
 - Bond Insurer
 - HUD
 - Four (4) SCO audits (RDA, Gas Tax, Fed/State Expenditures, Internal Controls)
- Montebello TRAN is placed – closed on November 10, 2011

Montebello's Continued Road to Recovery





Purpose of the Management Summary Report

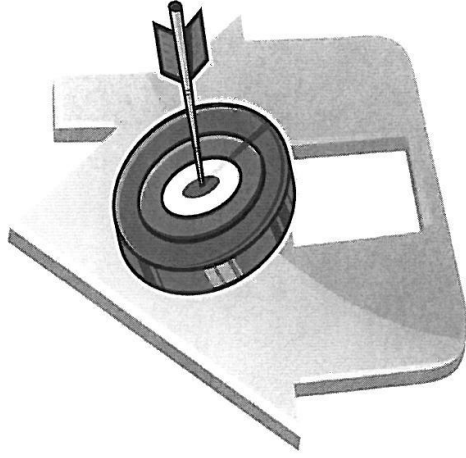
Serve as a blueprint for the next permanent City Administrator and current management team and consultants to ensure the City's financial success through a *comprehensive organizational approach*:

- Progress with improved financial management, accounting controls and cash flow measures
- Maintain pace of execution of the 5-year Plan, including key economic development projects
- Continue systemic organizational & operational improvements
- Revenue generating projects must be prioritized (resolution of Supreme Court challenge on Redevelopment due by Jan 15, 2012)
- Set agenda for February Mid-Year Financial Review

Montebello Must Focus on Economic Development



- **Real Estate Projects** (private sector & public-private) – new property taxes or tax increment from “RDA”
- **Retail** – sales tax & jobs (entry level)
- **Relocation / Expansion** – business tax & commercial jobs
- **Rooms** – hotel transient occupancy tax (TOT)



Montebello has used Redevelopment as the primary tool to increase the City's job base and taxes

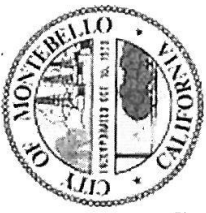
Must now act on Economic Development opportunities beyond the scope of Redevelopment

5-Year Plan Execution – Key Projects



- **Montebello Enterprise Funds**
 - Hilton Garden Inn Management Contract
 - Quiet Cannon finances
 - Golf Course management and finances
- **Costco Gas Station**
- **Montebello Hills**
- **SR-60 Transportation Corridor Projects (Long Term)**

Organizational & Operational Improvements – Near Term



- Secure permanent City Administrator
 - Strong leader
 - High integrity
 - Ability to motivate all changes
 - Capable of keeping pace of achieving 5-year recovery plan
 - Strong fiscal manager
 - Costs expected at around \$25,000 per month
 - Past Interim CA salary - \$195,000 plus 54% employee benefit costs
= \$300,000 or \$25,000 per month
 - Same as current Interim CA Team consisting of 2 Administrators

Organizational & Operational Improvements – Near Term



- **Installation of stand-alone Public Works Dept. with functions that are staffed and contracts competitively bid out**
 - **Competitively bid all major contracts & service agreements (>\$50,000) within a 3-yr period**
 - **Creation of 5-year Capital Improvement Program**
 - **Infrastructure investment and maintenance**
 - **Fleet management**
 - **Facilities maintenance**
 - **Equipment and vehicle replacement**

Improved Communication – Near Term



- **City Council and Staff cooperation**
 - Improved and standardized agenda staff reports
 - Agendas and minutes from commission meetings
 - Agendas from regional entities' meetings
- **Upgraded City website**
 - Easier to find important and timely information
 - Transparency regarding City issues and actions
 - Increased interaction with the community (e.g. complaint system)
- **Interdepartmental coordination**
- **City Council Code of Ethics**

Upgrade Financial Systems – Near Term (Partial List)



- Replacement / upgrade of the City's accounting system
- Implement cash receipts module and standardize cash collection procedures
- Consider alternative banking services provider to better serve City needs
- Consider new auditing services provider and standardize auditing
- Update petty cash controls
- Implement processes to ensure that payroll transactions are recorded in a timely manner
- Implement policies and procedures to segregate incompatible functions
- Establish and implement policies to restrict employee access to human resources and payroll systems as appropriate

Org. & Operational Improvements – Longer Term (Partial List)



- Departmental budget management

- Improved quality & consistency of reports

- Upgrade in technology throughout the organization (initial focus on Finance Department)

- Restore employee compensation to competitive levels

- Determine appropriate staffing to meet needs & develop administrative analyst team to work across departments

- Restore, create, and improve services to the community

Longer-Term



Other Operational Tasks – Longer-Term (Partial List)



Task	Department
Update of Municipal Code	City Admin.
Update Administrative Policies	City Admin.
Update Personnel Rules & Regulations	Human Resources
Update Job Classifications	Human Resources
Need for Comprehensive MOUs	Human Resources
General Plan Update	Comm. Dev.
Zoning Code Update	Comm. Dev.
Integrated Permitting System	Comm. Dev.
Geographic Information System (GIS)	Comm. Dev.
ADA compliance in the parks	Municipal Services

Summary of Needed Management Improvements



- Secure permanent City Administrator
- Installation of stand-alone Public Works Dept. with functions that are staffed and contracts competitively bid out
- Improved communication (e.g. agendas, website)
- Upgrade in technology throughout the organization, with initial focus on finance, accounting, and internal controls
- Restore employee compensation to competitive levels
- Determine appropriate staffing, develop team of analysts
- Restore, create, and improve services to the Community

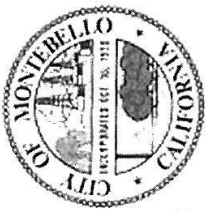


Next Steps in the Financial Recovery Plan

Focus on Mid-Year Financial Review

(February 2012)

Buckets of Opportunity – Revenue, Revenue, Revenue



In addition to financial scrutiny and ongoing execution of the FRP, the City must bring in money, focus on revenue measures:

- Costco – Gas Station Component
- Restaurant Development Opportunities
 - 701 W. Whittier Boulevard
 - 520-520 W. Whittier Boulevard
- Commercial Development Opportunities
 - 100 W. Washington Boulevard
- Enhanced Business Retention and Attraction Outreach Efforts
 - Coordination with all major shopping centers (Shops at Montebello, Montebello Town Square, Montebello Plaza, etc.)
 - Marketing efforts at the national ICSC Conference
 - Marketing of commercial properties
 - Ongoing communication with national and regional retail and restaurant chains

Management efficiency requires investment

Immediate "Wish-List" Cost Estimates*



Item	Description	Cost Range	Budgeted in 2011-12
Accounting System	Includes payroll & interdepartmental information sharing	\$500,000	No
Technology Upgrade (Citywide)	Work station computers, storage, server enhancements	\$381,500	No
General Plan Update	Complete efforts begun in 2005	\$240,000	No
Police Patrol Vehicles	Purpose is to get on a routine purchasing program	\$50,000 per year	No
Police Equipment Upgrades	License plate readers, vehicle computers	\$80,000	No
3 Type-1 Fire Engines	Current engines all purchased in 2003	Lease: \$200K/year Purchase: \$2.1 M	No
Fire Medical Gear	Defibrillators	\$75,000	No

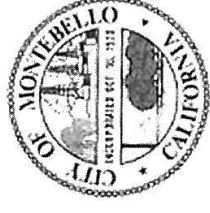
*Note: Preliminary figures, not a complete list

Mid-Year Financial Review (February 2012)



- **Evaluation of all audits and financial review**
- **Mid-year Review of FRP/Budget**
 - Target: Continue balanced, timely City budgets with reserves
 - Proactively manage City cash flow, gauge based on revenue production & savings from operations
 - Pay back TRAN
- **Meet requirements of all audits**
- **State Redevelopment reporting requirements per SCO audit**
 - Timely preparation of annual budget
 - Statement of Indebtedness
 - Annual Report
 - Independent Auditor's Report
 - Five Year Implementation Plan
 - Mid-year review of Implementation Plan
 - Low and moderate income housing database
 - Cash flow projections
- **Review and application of Willdan cost allocation study**
- **Upgrade financial systems (e.g. accounting systems, receipt/collections module)**

Montebello's Future: Next Steps for Success



What Has Held Montebello Back



- Over the past 5 years, Council political shifts and City Administrator turnover have resulted in bad administrative decisions and deficient administrative processes, and defective accounting practices
- Claims and stories re: bankruptcy, “off-the-books bank accounts with double payments” and corruption have not to date been found to be true or accurate, only misleading
- Seven audits in 6 months – Does Montebello need more to reinforce the already stated admission of poor past accounting, management and sloppy record keeping?
- We are living in a post “Bell” world and suspicion is pervasive. Montebello is not Bell.
- Montebello’s media coverage has been focused on the negative, but with TRAN placement, improved cash flow and adopted balanced budget there is an opportunity to turn it around

Montebello's Future is Bright – The Turnaround is Underway



- Montebello can be fixed...it is in process...takes time, leadership, and \$\$
- *Turnaround has started*
 1. Eliminated debt obligation between RDA and City (payment made prior to June 30)
 2. Updates to user fees and charges approved by City Council in June
 3. Clarified misleading prior issues such as “rogue, off-the-book” bank accounts
 4. Negotiation of a two-year extension of oil extraction levy
 5. Opened discussions with Costco on lease renewal and/or purchase options
 6. Evaluated Redevelopment Legislation, filed recommended continuation of redevelopment in Montebello, filed appeal to reduce annual payment to the State - \$1.24 million reduction approved = more RDA funds for City Economic Dev. efforts
 7. Various audits are being addressed with resolutions in process
 8. Positive credit rating and removal from negative watch from Moody's (City) and S&P (Redevelopment Agency)
 9. TRAN is sold

Next Steps



- **Adopt City Council Code of Ethics**
- **Recruit Permanent City Administrator**
- **Complete responses to various audits**
- **Prepare for mid-year budget review in February**
 - Will have completed audits, including City's own management audit, and obtained necessary feedback
 - Review revenues, expenses, status of execution on 5-yr FRP, including key economic development projects
 - Consider adjustments (e.g. tax increases, service cuts) as necessary to stay on track in advance of FY 2012-2013
 - Work on next iteration of FRP ("The Plan") – it is a dynamic document
- **Prioritize and implement operational improvements**
 - **Focus on financial management and other select improvements (e.g. stand-alone Public Works Department and competitive bidding)**
 - Most other items can and should wait for permanent City Administrator

City Administrator Recruitment is Underway

A collage of four black and white photographs of Montebello landmarks. The top photo shows a large industrial building with a sign that reads "MONTESANO". The bottom-left photo shows a modern city hall building with a sign that reads "CITY OF MONTEBELLO CITY HALL". The bottom-right photo shows a street sign for "Montebello" with the text "DO NOT REMOVE" and "FOR RESIDENTS". The top-right photo shows a street sign for "Montebello" with the text "DO NOT REMOVE" and "FOR RESIDENTS".

CITY OF
MONTEBELLO, CA

INVITES YOUR
INTEREST IN
THE POSITION OF

CITY
ADMINISTRATOR

**BOB MURRAY
& ASSOCIATES**
EXPERTS IN EXECUTIVE SEARCH

Much Has Been Done...There is Still Much to Do – Not Out of the Woods



- **Select qualified City Administrator**
- **Work hard to have positive mid-year review**
- **Pay back TRAN**
- **Resolve various audits**
- **Find the \$\$\$ to make investments in financial systems – will need it for the long haul**
- **Organizational changes – prioritize and implement**
- **Adopt City Council Code of Ethics – preferably before hiring permanent City Administrator**

Kosmont Companies

Thanks the City of Montebello



Special Thanks

<u>Department Heads & Staff</u>	<u>City Attorney's Office</u>	<u>Consultants & Advisors</u>
Fran Tucker-Schuyler	Arnold Alvarez-Glassman	Mike Kremer First Southwest Company
Mike Huntley	Matthew M. Gorman	Jeff Stava Nossaman LLP
David Biggs	David King	Don Hunt Fulbright & Jaworski LLP
Keith Breskin		Russ Trice Fulbright & Jaworski LLP
Andy Zageris		Richard Kornblith Fulbright & Jaworski LLP
		Don Parker RDA Reporting Solutions
		Joan Gladstone Gladstone International

*Also the City Administration Team, numerous other Department Heads, Staff, employment associations, citizens of Montebello, and others from the City family



Thank You

**State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250-5874**

<http://www.sco.ca.gov>